

## Message Text

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PAGE 01 OECD P 03531 01 OF 03 031854Z  
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LIMITED OFFICIAL USE SECTION 01 OF 03 OECD PARIS 03531

PASS CEA, TREAS, FRB

TAGS: OECD, ECON

SUBJECT: ECONOMIC AND DEVELOPMENT REVIEW COMMITTEE  
(EDRC) REVIEW OF THE NETHERLANDS

REF: A) EDR(77)2; B) STATE 17939; C) HAGUE 412;  
D) OECD PARIS 2127

1. SUMMARY: AT JANUARY 27 EDRC REVIEW OF NETHERLANDS,  
DUTCH DEL (LED BY VERBERG, MINISTRY OF ECONOMICS) PRE-  
SENTED REVISED GON ASSESSMENT OF OUTLOOK FOR 1977 WHICH  
WAS LESS OPTIMISTIC THAN OFFICIAL FORECASTS PREPARED IN  
SEPTEMBER, 1976. WHILE NEW FORECASTS NOT YET COMPLETED,  
DUTCH INDICATED THAT MAIN CHANGE WOULD BE DOWNWARD REVI-  
SION OF PROJECTED EXPORT VOLUME GROWTH TO REFLECT  
FACT THAT CURRENCY REALIGNMENT WITHIN "SNAKE" IMPLIED  
5-6 PERCENT APPRECIATION OF GUILDER IN 1977 (SEPTEMBER  
FORECAST ASSUMED NO CHANGE IN EFFECTIVE GUILDER RATE  
THIS YEAR). DUTCH STRESSED FIRM GON INTENTION OF MAIN-  
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PAGE 02 OECD P 03531 01 OF 03 031854Z

TAINING GUILDER WITHIN SNAKE. NEVERTHELESS, DIFFERENCE  
BETWEEN DUTCH AND SECRETARIAT PROJECTIONS OF GROWTH OF  
DUTCH EXPORT MARKETS AND RESULTING DIVERGENCE OF FORE-  
CAST EXPORT VOLUMES ACCOUNTED FOR NEARLY ALL OF DIFFER-  
ENCE BETWEEN SECRETARIAT AND DUTCH FORECASTS OF 1977  
GDP. BOTH SECRETARIAT AND DUTCH EXPECTED DECELERATION  
OF INFLATION IN 1977, CONTINUED SLACK IN LABOR MARKET

AND INCREASE IN CURRENT ACCOUNT SURPLUS. SECRETARIAT STATED THAT PROPOSED INVESTMENT STIMULATION PROGRAM WAS STEP IN RIGHT DIRECTION, BUT ADDED THAT FASTER GROWTH OF CONSUMPTION WOULD BE MORE EFFECTIVE MEANS OF GENERATING INVESTMENT. DUTCH INSISTED THAT ADDITIONAL FISCAL STIMULUS WOULD ONLY BE APPROPRIATE IN 1977 IF (A) EXPORT GROWTH (AND HENCE GDP GROWTH) PROVED TO BE SIGNIFICANTLY LESS THAN FORECAST, AND (B) THIS SHORTFALL OF EXPORTS WERE TO RESULT FROM WEAKNESS OF WORLD TRADE, RATHER THAN FROM FURTHER APPRECIATION OF GUILDER. MOREOVER, DUTCH SAID THAT EXISTENCE OF CURRENT ACCOUNT SURPLUS DID NOT ARGUE FOR MORE STIMULUS SINCE INCOME FROM GAS EXPORTS WHICH RESPONSIBLE FOR THIS SURPLUS MASKED BASIC WEAKNESS OF DUTCH ECONOMY. GON MONETARY POLICY WILL REMAIN GEARED TO KEEPING GUILDER IN SNAKE. END SUMMARY

2. SHORT TERM PROSPECTS; DOMESTIC OUTLOOK: DUTCH GAVE REVISED ESTIMATES FOR 1976 WHICH PUT GDP GROWTH FOR YEAR AT 4 PERCENT VS. 3.5 PERCENT FORECAST IN SEPTEMBER, WITH DIFFERENCE LARGELY ATTRIBUTABLE TO STRONGER THAN EXPECTED GROWTH OF PRIVATE CONSUMPTION SPENDING. IN CONTRAST, FOR 1977, DUTCH INDICATED THAT LATEST REASSESSMENT OF OUTLOOK FOR THIS YEAR PAINTED SOMEWHAT LESS OPTIMISTIC PICTURE THAN THAT CONTAINED IN SEPTEMBER FORECASTS. DOWNWARD REVISION OF FORECASTS OF EXPORT VOLUME GROWTH IN 1977 (BECAUSE OF ASSUMED APPRECIATION OF GUILDER, SEE PARA 8) WOULD, IN GON VIEW, RESULT IN REAL GDP GROWTH OF SOMEWHAT LESS THAN THE 4.1 PERCENT CONTAINED IN SEPTEMBER, 1976 FORECAST. DUTCH LIMITED OFFICIAL USE

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PAGE 03 OECD P 03531 01 OF 03 031854Z

MAINTAINED, HOWEVER, THAT SECRETARIAT'S MORE PESSIMISTIC PROJECTION OF GROWTH OF DUTCH EXPORT MARKETS AND OF DOMESTIC DEMAND WAS UNWARRANTED AND THAT SECRETARIAT FORECAST OF 3.5 PERCENT RISE IN REAL GDP WAS AN UNLIKELY OUTCOME.

3. DUTCH FELT THAT EFFECTS OF INVESTMENT STIMULUS PROGRAM (TO BE IMPLEMENTED APRIL 1, 1977) WOULD BE INSTRUMENTAL IN BRINGING ABOUT THE 7 PERCENT INCREASE IN REAL NON-RESIDENTIAL INVESTMENT SPENDING FORECAST BY GON FOR 1977. SEVERAL EDRC DELS NOTED THAT TERMINATION OF EXISTING INVESTMENT-SUPPORT MEASURES (E.G. ACCELERATED DEPRECIATION PROVISIONS) WOULD DILUTE STIMULATORY EFFECTS NEW PACKAGE. DUTCH ASSERTED THAT NET EFFECT OF ELIMINATING EXISTING MEASURES AND ADDING NEW ONE WOULD BE SIGNIFICANT INCREASE IN STIMULUS. FURTHERMORE, DUTCH NOTED THAT RECENT MILD ACCELERATION OF INVESTMENT SPENDING COULD WELL BE DUE FAVORABLE "ANNOUNCEMENT EFFECTS" OF NEW PROGRAM AND DID NOT (AS SUGGESTED BY

U.S. PER REF C) REFLECT FIRMS' PREFERENCE FOR EXISTING MEASURES.

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PAGE 01 OECD P 03531 02 OF 03 031916Z  
ACTION EUR-12

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LIMITED OFFICIAL USE SECTION 02 OF 03 OECD PARIS 03531

4. U.S. NOTED THAT PROPOSED "EXCESS PROFITS" (VAD) TAX HAD APPARENTLY HAD NEGATIVE IMPACT ON BUSINESS CONFIDENCE AND THUS COULD FURTHER WEAKEN POSITIVE EFFECTS OF INVESTMENT PROGRAM. DUTCH DID NOT ADDRESS QUESTION OF BUSINESS CONFIDENCE, BUT ONLY NOTED THAT VAD WAS BASED ON PRINCIPLE THAT DISTRIBUTION OF "EXCESS PROFITS" (MORE THAN LONG-TERM BOND RATE, PLUS 2 PERCENT FOR BUSINESS RISK) SHOULD BE DISTRIBUTED BETWEEN LABOR AND CAPITAL AND SHOULD NOT BE EXCLUSIVE PROPERTY OF SHAREHOLDERS.

5. SECRETARIAT ARGUED THAT DIRECT STIMULUS TO INVESTMENT WOULD HAVE MINIMAL EFFECT ON INVESTMENT SPENDING IN 1977 SINCE FIRMS WERE OPERATING AT ONLY 75 PERCENT OF CAPACITY. ON THE OTHER HAND, SECRETARIAT SUGGESTED THAT MEASURES TO BOOST CONSUMPTION DEMAND WOULD INCREASE UTILIZATION RATE AND AS A CONSEQUENCE WOULD HELP BRING FORTH INVESTMENT, INCREASE PROFITS AND REDUCE UNIT COSTS. DUTCH COUNTERED THAT INVESTMENT PACKAGE HAD MEDIUM TERM LIMITED OFFICIAL USE

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PAGE 02 OECD P 03531 02 OF 03 031916Z

RATHER THAN SHORT TERM FOCUS AND THAT, IN ANY CASE, INVESTMENT IN NETHERLANDS RESPONDED MORE TO COST AND PRICE DEVELOPMENTS THAN TO CHANGES IN DEMAND.

6. PRICES AND WAGES: GON ESTIMATES THAT CONSUMER PRICES ROSE BY 9 PERCENT IN 1976. HOWEVER, DUTCH POINTED OUT THAT, OF THIS INCREASE, 3.5 PERCENTAGE POINTS REPRESENTED CARRYOVER FROM 1975 AND THAT UNDERLYING RATE OF INFLATION DECELERATED TO ABOUT 6.5 PERCENT BY END OF YEAR. THEY INDICATED THAT OUTLOOK FOR WAGES IN 1977 WAS STILL HIGHLY UNCERTAIN BECAUSE OF CONTINUING DEADLOCK IN SECTORAL NEGOTIATIONS, BUT ADDED THAT EFFECT OF ASSUMING THAT GUILDER WOULD APPRECIATE BY 5-6 PERCENT IN 1977 WOULD BE TO LOWER PROJECTED RATE OF INFLATION TO 5.5 PERCENT COMPARED TO 6.5 PERCENT SEPTEMBER FORECAST. FINALLY, DUTCH STATED THAT SOCIAL INSURANCE FUNDS HAD RECORDED LARGER THAN EXPECTED SURPLUS IN 1976 AND THAT, CONSEQUENTLY, THERE MIGHT BE SCOPE FOR DECREASE IN EMPLOYER/EMPLOYEE CONTRIBUTIONS IN JANUARY, 1978 OR EARLIER WITH RESULTANT FAVORABLE EFFECTS ON COSTS, PROFITS AND PRICES.

7. UNEMPLOYMENT: SECRETARIAT EXPRESSED VIEW THAT DECLINE IN UNEMPLOYMENT IN LATE 1976 WAS LARGELY DUE TO SPECIAL FACTORS (E.G. EARLY RETIREMENTS, INDUCED BY RISE IN DISABILITY PAYMENTS) AND THAT FURTHER DECLINE IN 1977 WAS UNLIKELY. DUTCH STUCK TO PROJECTION THAT UNEMPLOYMENT WOULD DECLINE AND SAID THAT PROPOSED ADDITIONAL WAGE COST SUBSIDIES WOULD CONTRIBUTE TO THIS RESULT BY REDUCING INVESTMENT EMBODYING LABOR-SAVING TECHNOLOGY. NEVERTHELESS, THEY ADMITTED THAT RISK IN GON UNEMPLOYMENT FORECASTS WAS CONCENTRATED ON UPSIDE.

8. CURRENT ACCOUNT: GON'S SEPTEMBER FORECAST OF 8.5 PERCENT INCREASE IN EXPORT VOLUMES WAS BASED ON ASSUMPTIONS THAT: (A) DUTCH EXPORT MARKETS WOULD GROW BY 8

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PAGE 03 OECD P 03531 02 OF 03 031916Z

PERCENT AND (B) EFFECTIVE GUILDER EXCHANGE RATE WOULD NOT APPRECIATE, ON AVERAGE, BETWEEN 1976 AND 1977. HOWEVER, DUTCH NOTED (AS HAD SECRETARIAT IN REFD0C) THAT CURRENCY REALIGNMENT WITHIN "SNAKE" IN OCTOBER 1976 LEFT END-1976 GUILDER EXCHANGE RATE 5-6 PERCENT ABOVE 1976 AVERAGE WHICH, ASSUMING NO CHANGE IN RATE DURING YEAR, IMPLIED AVERAGE APPRECIATION OF THIS AMOUNT IN 1977

WHICH COULD RESULT IN SOME LOSS IN MARKET SHARES. (GON ASSUMES THAT GUILDER WILL NOT APPRECIATE FURTHER DURING 1977.)

9. DESPITE SLOWDOWN IN OECD AREA GROWTH IN SECOND HALF OF 1976, DUTCH FELT THAT PROBABLE REFLATIONARY ACTION IN U.S. (AND TO LESSER EXTENT IN JAPAN AND POSSIBLY IN GERMANY) SUPPORTED CASE AGAINST DOWNWARD REVISION OF PROJECTED 8 PERCENT GROWTH IN DUTCH EXPORT MARKETS AND FORECAST 7.5 PERCENT GROWTH OF EXPORT VOLUMES. SECRETARIAT EXPRESSED VIEW THAT ADDITIONAL POLICY MEASURES IN MAJOR COUNTRIES WOULD HAVE MINIMAL EFFECT ON WORLD TRADE IN 1977 AND SAW NO REASON TO CHANGE ITS FORECAST OF 6.25 PERCENT INCREASE IN DUTCH MARKETS AND 4.5 PERCENT RISE IN EXPORT VOLUMES. SECRETARIAT AND DUTCH AGREED THAT WIDE DIVERGENCE BETWEEN THEIR RESPECTIVE PROJECTIONS OF GROWTH OF EXPORT VOLUMES WOULD EXPLAIN VIRTUALLY ALL OF DIFFERENCE BETWEEN THEIR FORECASTS OF GDP GROWTH. BECAUSE OF SECRETARIAT'S LESS BUOYANT ASSESSMENT OF GROWTH OF DOMESTIC DEMAND, ITS FORECASTS FOR IMPORT GROWTH LIE BELOW THOSE OF GON WITH RESULT THAT DUTCH AND SECRETARIAT AGREED THAT CURRENT

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PAGE 01 OECD P 03531 03 OF 03 031904Z  
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LIMITED OFFICIAL USE SECTION 03 OF 03 OECD PARIS 03531

ACCOUNT SURPLUS WOULD RISE TO 7 BILLION GUILDER IN 1977  
FROM SURPLUS OF 6 BILLION GUILDER IN 1976.

10. ECONOMIC POLICY: WHILE AGREEING ON CURRENT ACCOUNT FORECASTS FOR 1977 DUTCH AND SECRETARIAT DIFFERED ON POLICY CONCLUSIONS TO BE DERIVED THEREFROM. SECRETARIAT SUGGESTED THAT IF EXPORTS (AND HENCE GROWTH) WERE TO TURN OUT WEAKER THAN GON FORECASTS, ADDITIONAL FISCAL STIMULUS SHOULD BE APPLIED AND THAT CURRENT ACCOUNT SURPLUS GAVE GON NECESSARY FLEXIBILITY TO TAKE SUCH ACTION. CITING CONCLUSIONS OF 1976 OECD MINISTERIAL, SECRETARIAT NOTED RESPONSIBILITY OF COUNTRIES IN STRONG EXTERNAL POSITION FOR MAINTAINING GROWING EXPORT MARKETS FOR WEAKER COUNTRIES. DUTCH ANSWERED THAT, (A) SURPLUS RESULTED FROM EXPORTS OF NATURAL GAS; (B) CONTRIBUTION TO CURRENT ACCOUNT SURPLUS OF NATURAL GAS PROJECTED TO BEGIN DECLINE IN 1978 WITH SHARP DROP OFF BEGINNING IN 1980 AND; (C) NATURAL GAS EXPORT RECEIPTS MASKED BASIC STRUCTURAL WEAKNESS OF DUTCH ECONOMY. DUTCH CONCLUDED LIMITED OFFICIAL USE

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PAGE 02 OECD P 03531 03 OF 03 031904Z

THAT CURRENT ACCOUNT SURPLUS DID NOT IMPLY NEED FOR FURTHER REFLATION. FURTHERMORE, DUTCH FELT THAT IF EXPORT SHORTALL WERE RESULT OF GUILDER APPRECIATION, APPROPRIATE POLICY RESPONSE WOULD BE TO TAKE FURTHER ACTION ON COST/PRICE SIDE; WHEREAS, THEY CONCEDED, IF SHORTFALL RESULTED FROM WEAK TREND IN EXPORT MARKETS SOME REFLATIONARY STEPS COULD POSSIBLY BE APPROPRIATE.

11. DUTCH EXPLAINED RATIONALE FOR "1 PERCENT POLICY" (OUTLINED REFS C AND D). SOME DELS NOTED THAT GOAL OF REDUCING GROWTH OF PUBLIC SECTOR BURDEN ON ECONOMY WAS LESS THAN AMBITIOUS SINCE BURDEN WOULD HAVE GROWN BY ONLY 1.75 PERCENT IN ABSENCE OF NEW MEASURES. DUTCH SAID THAT IN NETHERLANDS CONTEXT, EVEN SUCH SMALL REDUCTION IN GROWTH RATE OF PUBLIC SECTOR WAS A MAJOR FEAT.

12. DUTCH EMPHASIZED THAT PRIMARY AIM OF MONETARY POLICY WOULD BE TO HOLD GUILDER WITHIN SNAKE. SEVERAL EDRC DELS WERE SKEPTICAL OF GON'S ABILITY TO INDUCE CAPITAL OUTFLOWS IN AMOUNTS SUFFICIENT TO PREVENT APPRECIATION OF GUILDER. DUTCH ASSERTED THAT MONETARY POLICY TOOLS WERE ADEQUATE TO TASK, BUT AGREED THAT ABSORPTION OF PRESENTLY EXISTING EXCESS LIQUIDITY (WHICH EDRC FELT POSED SIGNIFICANT INFLATIONARY RISK FOR 1977) WITHOUT INDUCING RISE IN INTEREST RATES WOULD REQUIRE CONSIDERABLE INGENUITY.

13. QUESTIONS RAISED PARAS 2, 3, 4 AND 5 REF B  
ADDRESSED PARAS 6, 12, 8 AND 10. POINTS RAISED PARAS

1-7 REF C DISCUSSED PARAS 1, 11, 3, 8, 6 AND 4.  
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## Message Attributes

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